

PENSION JUSTICE NPC

UNDERSTANDING THE NEW TWO-POT RETIREMENT SYSTEM

The Minister of Finance announced in the 2023 Budget Speech, that a **TWO-POT SYSTEM** for pension funds will be implemented on 1 April 2024.

The current system: A one-pot system

- Currently, workers and employers contribute to a Pension Fund or Provident Fund. That Fund invests the total collected money of all the workers.
- With a bigger collective investment, each worker gets a bigger return on their investment compared to if they were just saving privately, by themselves. This is partly because of lower costs associated with larger investments and administering them.
- The money goes into one pot per worker, and workers receive their investments only when they retire, resign or are fired.

The system of collective investment will **NOT** change. Only the time when workers can access their Fund benefits will change

WHY CHANGE THE ONE-POT SYSTEM?

The one-pot system is very convenient for Fund administrators and for employers. It also helps optimise fund returns on investment. But it is not suitable for the financial reality which most workers in South Africa face.

- Workers are only able to access the money in the fund if they resign, retire or are fired. Unlike rich people who have many pots of money, workers cannot access their own money when they need it because it is locked away in one pot for retirement.
- When the time comes to send a child to university or to fight bank repossession, to pay for a house, or to repay debt, workers do not have the money in their bank account, and they do not have separate savings accounts. The pension savings is all they have.
- During COVID, the effect of this was very harshly felt by workers who were financially distressed and chose early access to their retirement fund savings.
- This meant that many workers who still have stable employment have been resigning early from their jobs when they desperately need a lump sum of money.

Unions pushed for some form of early access to retirement fund savings without resigning.

Why is resigning early financially bad for workers?

ONE: Workers lose their jobs when they resign. With increasing casualisation, labour broking, temporary employment contract and wage reductions, these workers either struggle to find new jobs with retirement benefits, or they do not find jobs at all.

TWO: The earlier workers take money out of their pension or provident fund, the less the payout is. The amount workers get for early resignation is less than if they retired at retirement age. In addition, the early withdrawal of a lump sum would be subject to tax. The worker's tax rate is likely to be higher than upon retirement.

THREE: Workers also lose most or all their savings for their retirement and risk having no money to support them in old age. This in turn can put strain on the government's old age pension system.

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THE TWO-POT SYSTEM

How will the two-pot system work?

The two-pot system will allow workers to draw a certain percentage of their retirement savings before retirement or leaving employment, and will “lock in” the rest for retirement.

According to the latest Bill published in June 2023, the new system will be that from 1 March 2024:

- Workers can make a once-off withdrawal from their retirement fund of between R2 000 and R25 000, provided the amount is no more than 10% of their vested savings on 29 February 2024.
- One-third of new contributions from 1 March 2024 onwards will be invested in the worker’s “savings pot” and two-thirds will be “locked in” in the worker’s “retirement pot”
- Once a year, workers can choose to withdraw their all or some of their one-third (their savings pot). If they choose to withdraw, the minimum amount is R2 000.
- Importantly, there is no “means test” or other criteria to withdraw from the savings pot.

What people say in support of the two-pot system

- Workers will be able to access a portion of their retirement money early, and that they can do this without having to resign and take out all their retirement savings.
- This acknowledges the reality that workers are facing: that they need access to at least some of their money to support them at present, before they can even think about supporting themselves in the future.

What people say against the two-pot system

- Workers who do not resign will now have additional early access to their savings and anyone who withdraws some of their money before retirement will have less at retirement.
- It is against the core principle of pension funds: to provide for long-term savings for retirement. Fund investments, liquidity and administration costs are set up in a way to support and optimise, this long-term objective. Funds would therefore need to change their investment strategies to include more short-term components to ensure that they can fund these constant withdrawals. This could lower investment returns for members. This will also increase administration costs which members pay.
- Workers will be taxed at their personal tax rate on every withdrawal.

What is happening between now and 1 April 2024?

- There are still issues that have not been resolved by the Department of Finance.
- The “Retirement Industry” needs time to prepare for the implementation. They can only do this after the laws have been passed by parliament.
- In June 2023, draft legislation (a bill) on the two-pot system was published.